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Technical notes

Note by the Secretary-General

Addendum

Technical note No. 7:* Existing proposals on bilateral and multilateral investment agreements and practices as regards codes of conduct for transnational corporations and Governments with respect to foreign direct investment

I. Introduction

1. International rule-making on or directly relating to investment issues is multifaceted and spans the bilateral, regional, interregional and multilateral levels. It can take the form of binding or voluntary instruments creating different degrees of obligations.[1]

2. **Bilateral** investment treaty making has been particularly active over the past decade.[2] Bilateral investment treaties (BITs) are designed to promote, protect and facilitate foreign investment. Since the adoption of the first BIT in 1959, the number of such treaties had grown steadily to 385 by the end of 1989 and jumped to 1,941 by the end of 2000. Parallel to BITs, countries are also increasingly concluding agreements for the avoidance of double taxation, the number of which had reached 2,118 by the end of 2000. They address, among other things, the allocation of taxable income, inter alia, with a view to reducing incidents of double taxation. In recent years, bilateral trade agreements have also increasingly addressed

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investment issues (for example, agreements between Australia and New Zealand, Japan and Singapore, Canada and Chile, and Mexico with Chile, Costa Rica and Nicaragua respectively), as have the association agreements of the European Community.

3. BITs constitute to date the most widely used instrument for the international protection of foreign direct investment (FDI). Their main provisions typically deal with the scope and definition of foreign investment (which in most cases includes tangible and intangible assets, direct as well as portfolio investments, and existing as well as new investments); entry of investments; national and most-favoured-nation treatment; fair and equitable treatment; guarantees and compensation in respect of expropriation and compensation for war and civil disturbances; guarantees of free transfer of funds and repatriation of capital and profits; subrogation on insurance claims; and dispute settlement provisions, both State-to-State and investor-to-State. In addition, some BITs include provisions regarding transparency of national laws; performance requirements; entry and sojourn of foreign personnel; general exceptions; and extension of national and most-favoured-nation-treatment to the entry and establishment of investments. The exact content of BIT provisions, however, varies considerably, even between BITs signed by the same country.[3] BITs have traditionally been negotiated between developing countries seeking to attract international investment and developed countries as the principal homes to foreign investors. Developing countries, as hosts to FDI, concluded BITs in order to create a favourable climate and in some cases to become eligible to participate in political risk insurance programmes organized by capital-exporting countries. The BIT network grew rapidly in the 1990s, as more developing countries and economies in transition signed treaties with a wider range of developed countries and started to sign BITs between themselves.

4. At the **regional** level, only a few instruments are entirely devoted to investment. Particularly well known are the Framework Agreement on the Association of Southeast Asian Nations (ASEAN) Investment Area and the Andean Community's Decision 291. In addition, regional trade agreements have included in recent years investment-related provisions of various kinds. The North American Free Trade Agreement (NAFTA), the Southern Cone Common Market (MERCOSUR) Protocols and the Common Market for Eastern and Southern Africa (COMESA) Treaty are examples. The general aim of these agreements is to create a more favourable investment climate, with a view to increasing the flow of investment within or between regions.

5. At the **interregional** level, the Organisation for Economic Cooperation and Development (OECD) Declaration on International Investment and Multinational Enterprises is perhaps the best-known example. It sets forth non-binding principles and standards addressed to both Governments and enterprises in a framework designed to create a favourable climate for international investment and maximize the positive contribution that transnational corporations (TNCs) can make to economic, social and environmental progress. The OECD Guidelines for Multinational Enterprises, which form an integral part of the Declaration, make recommendations to enterprises on a wide range of business activities, including employment and industrial relations, environment, consumer interests, combating bribery, information disclosure, science and technology, competition and taxation. Their aim is to help TNCs operate in harmony with government policies and with societal expectations wherever they operate. Revised and updated in June 2000, in consultation with business, labour and representatives of other non-governmental bodies, the OECD Guidelines are supported by implementation procedures in the participating countries. The other parts of the Declaration contain commitments by adhering Governments to provide national treatment to established foreign affiliates, to avoid imposing conflicting requirements on enterprises and to cooperate regarding investment incentives and disincentives. All 30 OECD member countries and 3 non-OECD countries (Argentina, Brazil and Chile) adhere to the Declaration. OECD encourages other countries to join the Declaration, and seven countries (Estonia, Latvia, Lithuania, Israel, Singapore, Slovenia and Venezuela) are engaged in adherence proceedings.

6. The OECD Code of Liberalisation of Capital Movements and Code of Liberalisation of Current Invisible Operations constitute legally binding rules, stipulating progressive, non-discriminatory liberalization of capital movements, the right of establishment and current invisible transactions (mostly services). All non-conforming measures must

be listed in country reservations against the Codes. The Codes are implemented through policy reviews and country examinations, relying on "peer pressure" to encourage unilateral rather than negotiated liberalization. The Codes were initially adopted in 1961 but have since been revised and expanded in scope. Important recent additions were the right of establishment (1986) and cross-border financial services (1992). For most member countries, remaining reservations against the obligations set out in the Codes relate to FDI, the purchase of real estate by non-residents and the prohibitions of certain types of securities operations.

7. From 1995 until 1998, negotiations on a Multilateral Agreement on Investment (MAI) took place at OECD. Negotiating countries consisted of all OECD members plus eight other economies from South America, Europe and Asia. The negotiations were unsuccessful.

8. The Energy Charter Treaty and the Asia-Pacific Economic Cooperation (APEC) Non-Binding Investment Principles are other important instruments spanning more than one region.

9. At the **multilateral** level, a number of rules bear on international investment, some binding, others not. The World Trade Organization Agreement on Trade-related Investment Measures (TRIMs),[4] which entered into force on 1 January 1995, prohibits any TRIM that is inconsistent with the provisions of article III or article XI of the General Agreement on Tariffs and Trade (GATT) 1994. The World Trade Organization General Agreement on Trade in Services (GATS) sets out general principles, obligations, commitments and exemptions governing international trade in services. The World Trade Organization Agreement on Subsidies and Countervailing Measures provides a comprehensive framework of disciplines in this area.

10. The Multilateral Investment Guarantee Agency (MIGA) offers insurance against political risks to foreign investors, and the International Centre for Settlement of Investment Disputes (ICSID) offers a forum for the settlement of investment disputes. Over the past decade, MIGA has provided over $8 billion in guarantees covering investments in nearly 80 countries and facilitating investments in excess of $40 billion. ICSID has registered a total of 85 arbitration cases, of which 42 were brought to ICSID under bilateral and multilateral investment protection treaties. The World Bank Guidelines on the Treatment of Foreign Direct Investment, submitted to the Development Committee for its consideration in September 1992, are a non-binding instrument.

11. The International Labour Organization (ILO) Tripartite Declaration of Principles concerning Multinational Enterprises and Social Policy addresses issues related to employment, training, conditions of work and life, and industrial relations, and also includes a procedure for the examination of disputes concerning the application of this agreement by means of interpretation of its provisions. Of relevance also are the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices (A/C.2/35/6, annex), which provide non-binding principles and rules for the adoption, improvement and enforcement of appropriate legislation and procedures for the control of restrictive business practices by domestic firms as well as TNCs. Efforts during the 1980s to adopt a United Nations code of conduct on transnational corporations were unsuccessful.

12. The 1999 Global Compact of the United Nations Secretary-General takes a different approach. It is not a regulatory instrument or code of conduct, but a value-based platform designed to promote institutional learning. It provides a framework for better interaction between TNCs and host countries, utilizing transparency and dialogue to identify and disseminate good practices based on universal principles. The Compact encompasses nine such principles, drawn from the Universal Declaration of Human Rights,[5] the ILO's Declaration on Fundamental Principles and Rights at Work and the principles contained in the Rio Declaration on Environment and Development.[6] The Compact asks companies to act on these principles in their own corporate domains. The Compact also supports efforts to enhance the contribution of FDI to development.

II. Proposals

13. It is virtually impossible to establish a comprehensive listing of proposed bilateral instruments containing investment-related provisions; in particular, a large number of BITs and double taxation agreements are negotiated every year. At the regional and multilateral levels a number of initiatives are announced, and are under discussion or negotiation;

some details are provided below on a selected number of them. There are also a number of proposals by groups of civil society as regards international investment instruments.[7]

Free Trade Area of the Americas

14. The Free Trade Area of the Americas (FTAA) process was initiated at the First Summit of the Americas held in Miami in December of 1994.[8] From September 1995 to March 1998, a total of 12 working groups, including a Working Group on Investment, met on a regular basis to prepare the negotiations, which were launched at the Second Summit held in Santiago, Chile, in April 1998. At their Third Summit held in Quebec City from 20 to 22 April 2001, the leaders of FTAA participating countries (in the Declaration of Quebec City, 22 April 2001), directed their ministers responsible for trade "to ensure that negotiations of the FTAA Agreement are concluded no later than January 2005 and to seek its entry into force as soon as possible thereafter, but in any case, no later than December 2005".

15. Countries are currently negotiating on a draft agreement dated 3 July 2001. As part of the draft FTAA Agreement, an Investment Chapter is being negotiated. The Negotiating Group on Investment is called upon to develop a framework incorporating comprehensive rights and obligations on investment, taking into consideration the substantive areas already identified by the earlier Working Group on Investment, as well as to develop a methodology to consider potential reservations and exceptions to the obligations. The Negotiating Group on Investment has completed two negotiating rounds and prepared a consolidated draft text of the Investment Chapter. Issues covered in this preliminary version of the Investment Chapter include scope, basic definitions, national treatment, most-favoured-nation treatment, fair and equitable treatment, performance requirements, key personnel, transfers, expropriation, compensation for losses, general exceptions and reservations, dispute settlement, transparency, and the commitments neither to relax domestic environmental laws nor to relax domestic labour laws to attract investment. At their sixth meeting held in Buenos Aires, on 7 April 2001, FTAA Ministers of Trade agreed to publish the first draft of the FTAA Agreement. They instructed the Negotiating Groups "to continue working under the general principle that any delegation has the right to present the text proposals it deems relevant for the effective progress of the process, which may eventually be placed in brackets (Ministerial Declaration, annex I, General Instructions, para. 1)". Ministers of Trade also recognized that "environment and labour should not be utilized as conditionalities nor subject to disciplines, the non-compliance of which can be subject to trade restrictions or sanctions (ibid.)". FTAA Ministers of Trade instructed the Negotiating Groups "to intensify efforts to resolve existing divergences and reach consensus, with a view to eliminating the brackets from draft texts, to the maximum extent possible" (Ministerial Declaration, para. 10) and to submit a new version of their respective chapter no later than eight weeks prior to the next Ministerial Meeting, to be held in Ecuador in October 2002. To comply with the second part of its mandate, namely, to develop a methodology to consider potential reservations and exceptions, the Negotiating Group on Investment was instructed "to submit ... its recommendations on modalities and procedures ... in order to initiate negotiations no later than 15 May 2002 (ibid., annex I, sect. C, para. 1)".

SAARC Regional Agreement on Investment Promotion and Protection

16. The South Asian Association for Regional Cooperation (SAARC) comprises Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka. At the seventh meeting of the Committee on Economic Cooperation of SAARC, held in 1996, the Council of Ministers agreed to initiate specific steps to promote and protect investment and joint venture efforts. Pursuant to that decision, a meeting on Promotion and Protection of Investment had been held in New Delhi on 29 and 30 September 1997 during which modalities for increasing intraregional investment were considered and a draft "SAARC Regional Agreement on Investment Promotion and Protection" was circulated. At the eleventh meeting of the Committee, held in Dhaka, in February 1999, it was decided to convene a second meeting on Promotion and Protection of Investment in India to examine the draft investment agreement and consider the possibility of establishing a SAARC Arbitration Council. A Standing Group on Standards, Measurement and Quality Control has been constituted with a view towards upgrading national standards and evolving harmonized regional standards.

In addition, a Regional Agreement on the Avoidance of Double Taxation is being considered.

Southern African Development Community (SADC) Protocol on Finance and Investment

17. The Southern African Development Community (SADC) includes the following countries: Angola, Botswana, the Democratic Republic of the Congo, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, the United Republic of Tanzania, Zambia and Zimbabwe. The Protocol, drafted in March 1998, sets out the basic principles of investment policy. These include, among others, that the pace of privatization in the region should be increased and private-public partnerships encouraged; that foreign and domestic investors should have equal access; that simple, transparent and non-discriminatory procedures for the approval, entry and operation of investment needed to be established; and that investment promotion agencies should shift attention from incentives measures towards policy and administrative reform in order to attract investment.

Resolution of the European Parliament on European Union (EU) Standards for European Enterprises Operating in Developing Countries: Towards a European Code of Conduct

18. This resolution was adopted on 15 January 1999. In it, the European Parliament reiterated its request to the European Commission and the European Council "to make proposals, as a matter of urgency, to develop the right legal basis for establishing a European multilateral framework governing companies' operations worldwide and to organize for this purpose consultations with companies' representatives, the social partners and those groups in society that would be covered by the code" (para. 11).[9]

The proposal of the Group of Seven Finance Ministers to the Group of Eight Heads of State and Government

19. At the 2001 Genoa Summit, the Group of Seven (G-7) Finance Ministers made the following proposal:

"The implementation of investment-related best practices as well as the development of international principles, codes and standards can provide guidance for and underpin domestic reform efforts by developing countries. We call on the international financial institutions (IFIs) and other relevant multilateral bodies to intensify their effort to promote implementation of international codes and standards in the context of the policy dialogue with partner countries. We call on the World Bank, in cooperation with other relevant bodies, to step up its work to produce ROSC (Reports on the Observance of Standards and Codes) assessment modules of compliance with corporate governance and accounting standards. Progress in the implementation of standards must be visible in order to allow for the private sector actors to adjust their risk assessment and risk ratings. At the multilateral level, a stable and non-discriminatory investment regime could be brought about and maintained through the establishment of a high-standards framework of investment rules. We also encourage the continued discussion on investment in the World Trade Organization working group and urge the relevant international institutions, in particular the World Bank, OECD, the World Trade Organization and UNCTAD, to continue their cooperative efforts focusing on best practices with respect to the protection of property rights, investor protection, investment policies, competition-enhancing policies and transparent tax regimes."[10]

Review of the operation of the World Trade Organization Agreement on Trade-related Investment Measures (TRIMs)

20. The TRIMs Agreement provides in article 9 for a review of its operation by the Council for Trade in Goods no later than five years after the date of entry into force of the Agreement Establishing the World Trade Organization. Article 9 envisages that in the context of that review consideration shall be given to whether the Agreement should be complemented with provisions on investment policy and competition policy. The Council had initiated this review in October 1999, in connection with which it recently decided to

request the secretariats of the World Trade Organization and UNCTAD to prepare a study of the use of TRIMs and other performance requirements and their effects on trade and development. In the context of the preparatory process for the World Trade Organization Third Ministerial Conference held in Seattle, proposals were made in 1999 regarding possible changes to the TRIMs Agreement. Some of these proposals would have expanded the scope of the Agreement while others would have provided for exemptions for developing countries and for a general extension of the period within which developing countries were required to eliminate TRIMs of which they had notified to the Council. In July 2001, the Council for Trade in Goods adopted decisions under article 5.3 of the TRIMs Agreement that extended the transition period until 31 December 2001 and provided for the possibility of a further extension of that period until 31 December 2003. These decisions apply to Argentina, Colombia, Malaysia, Mexico, Pakistan, the Philippines and Romania. At the same time, the General Council adopted a waiver under article 9 of the World Trade Organization Agreement that accorded a similar extension of the transition period to Thailand.

The General Agreement on Trade in Services (GATS): built-in agenda

21. As part of the built-in agenda of the Uruguay Round of multilateral trade negotiations agreements, negotiations on services have resumed. The first stage of negotiations on services was completed at a stocktaking at the March 2001 meeting of the Council for Trade in Services, which resulted in the adoption of the "Guidelines and Procedures for the Negotiations on Trade in Services" (S/L/93). These guidelines emphasize development aspects as part of the objectives and principles for negotiations. The "request and offer" approach in the negotiations remains the main method, but other approaches may also be utilized. More than 80 proposals have been submitted to the Special Session of the Council, the majority of them by developed countries. The review of these proposals is at the core of the services negotiations leading into the World Trade Organization Ministerial Conference in Doha.

Further discussions on international investment matters in the World Trade Organization

22. The 1996 World Trade Organization Ministerial Conference, held in Singapore, agreed to begin work of an analytical nature on the "Relationship between trade and investment". The World Trade Organization Working Group on the Relationship between Trade and Investment, established to undertake this work, examines the links between trade and investment (with regard to FDI and foreign portfolio investment) from several angles, including (a) the implications of the relationship between trade and investment for development and economic growth; (b) the economic relationship between trade and investment; (c) stocktaking and analysis of existing international instruments and activities regarding trade and investment; and (d) the advantages and disadvantages for World Trade Organization members of bilateral, regional and multilateral rules on investment.

23. At the 1999 World Trade Organization Ministerial Conference in Seattle, several World Trade Organization members from developed countries, supported by some developing countries, proposed that a new multilateral framework of rules be negotiated in the World Trade Organization on foreign investment, to complement BITs and regional investment arrangements where these already existed. No consensus on these proposals was reached in Seattle.

24. Discussions among members on this subject continue in the World Trade Organization (including in the Working Group). While the Working Group has concentrated on continuing its examinations of the economic and development impact of FDI, in the context of discussions in the World Trade Organization General Council to prepare for the fourth World Trade Organization Ministerial Conference, a number of members have proposed that negotiations be launched on multilateral investment rules in the World Trade Organization. Other members have opposed this proposal. Other proposals that were made concern a plurilateral approach to the issue of investment in the World Trade Organization, and a continuation of the study process before entering into discussions of elements for the possible inclusion of investment on the World Trade Organization agenda could be considered. As of the writing of the present technical note, no consensus had been reached.

25. In the light of the multitude and variety of proposals and instruments under discussion and negotiation, the Secretary-General proposed in his report to the Preparatory Committee for the High-Level International Intergovernmental Event on Financing for Development at its second substantive session (A/AC.257/12) that "Member States should consider the convening of ad hoc global hearings to discuss the issues surrounding international investment agreements, in particular the extent to which such agreements can further the development of developing countries" (see boxed boldface text between paras. 51 and 52).

III. Bibliography

26. While there is a considerable literature on existing investment instruments, the literature on proposals for such instruments is limited. UNCTAD regularly reports on developments in this area in its annual *World Investment Reports*. A number of key issues are also addressed in UNCTAD's Series on Issues on International Investment Agreements (which has covered so far: illicit payments; home country operational measures; host country operational measures; social responsibility; environment; transfer of funds; employment; taxation; international investment agreements: flexibility for development; taking of property; trends in international investment agreements: an overview; lessons from the Multilateral Agreement on Investment (MAI); national treatment; fair and equitable treatment; investment-related measures; most-favoured-nation treatment; admission and establishment; scope and definition; transfer pricing; and foreign direct investment and development). The executive summaries of these studies are available on the Internet (at http://www.unctad.org/iia).

27. Useful background information can also be found in:

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Notes

[1] For a complete collection of existing instruments in this area see UNCTAD (1996, 2000a and forthcoming).

[2] For a survey of the existing network of BITs, see UNCTAD (2000b).

[3] For an in-depth comparative analysis of BIT clauses, see UNCTAD (1998).

[4] See *Legal Instruments Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, done at Marrakesh on 15 April 1994* (GATT secretariat publication, Sales No. GATT/1994-7).

[5] General Assembly resolution 217 A (III).

[6] *Report of the United Nations Conference on Environment and Development, Rio de Janeiro, 3-14 June 1992*, vol. I, *Resolutions Adopted by the Conference* (United Nations publication, Sales No. E.93.I.8 and corrigendum), resolution, annex I.

[7] For examples, see UNCTAD (1996, 2000a, forthcoming).

[8] This initiative involves the following 34 countries: Antigua and Barbuda, Argentina, the Bahamas, Barbados, Belize, Bolivia, Brazil, Canada, Chile, Colombia, Costa Rica, Dominica, the Dominican Republic, Ecuador, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Saint Lucia, Saint Kitts and Nevis, Saint Vincent and Grenadines, Suriname, Trinidad and Tobago, Uruguay, the United States of America and Venezuela.

[9] UNCTAD (2000a).

[10] Paragraph 24 of the report on "Debt relief and beyond", transmitted by the Group of Seven Finance Ministers to the Group of Eight Heads of State and Government at the Group of Eight Summit held in Genoa in July 2001.